Acquisition of Swiss real estate by foreign buyers

Swiss real estate market

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- The legal framework, financing arrangements, and taxes and duties payable must all be taken into account before embarking on a purchase.
- Property prices are linked to factors including distance from the nearest economic center and the income tax burden.
- Prices of owner-occupied homes have been rising much more briskly since 2020. Over the long term, price trends are closely tied to household incomes.

Source: Anita Affentranger

Switzerland's quality of life is among the highest anywhere in the world, with three Swiss cities regularly featuring in the top ten spots in the Mercer Quality of Living Rankings. The country's reliable legal system, stable political institutions and strong economy are all incentives to invest in Swiss real estate. This report covers the key considerations that foreign buyers need to be aware of when purchasing a property in Switzerland.

Legal considerations

The law governing property purchases is dependent on the buyer's residence permit status.

The rules on who can purchase a property in Switzerland are laid down in an act called the "Lex Koller." Citizens of EU and EFTA states are treated identically to Swiss buyers when purchasing real estate. Citizens of other countries who hold a C permit are also exempt from any property-buying restrictions. Non-EU or EFTA citizens with a B permit are only allowed to purchase a main or vacation home. Foreign nationals without a residence permit may only buy a second or vacation home. Only EU/EFTA citizens or holders of C permits are allowed to buy multi-family dwellings. There are no restrictions applying to commercial property.

Who can buy Swiss real estate?

Overview of the legal framework (Lex Koller)

Origin	Resid. permit	**First home***	**Second home**	**Holiday home**	**Multi-family house**	**Commerc. spaces**
Persons **domiciled** in Switzerland						
EU/EFTA	C I B	allowed	allowed	allowed	allowed	allowed
Non-EU/EFTA	C	allowed	allowed	allowed	allowed	allowed
Non-EU/EFTA	B	permit required (1)	not allowed	permit required (2)	not allowed	allowed
Persons **not domiciled** in Switzerland						
EU/EFTA		not allowed	permit required (3)	permit required (2)	not allowed	allowed
Non-EU/EFTA		not allowed	permit required (3)	permit required (2)	not allowed	allowed

allowed | permit required | not allowed

* Incl. construction land, construction needs to begin within a year
(1) For self-occupation only, can be kept if domicile changes
(2) Quota of max. 1,500 in Switzerland split across cantons
(3) Only if close connection exists, not to rent, has to be sold within 2 years if not

Source: UBS

No requirement to sell when moving out

Foreign owners are not required to sell up when moving out of or within Switzerland. They are free to use the property as a second or vacation home or to rent it to a third party, even if they buy a new main home. It would be breaking Swiss law, however, for them to buy a new main home with no intention of occupying it. Once a property has

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been purchased in accordance with the law, no further permissions are required for it to pass to the owners' heirs upon their death.

Financing

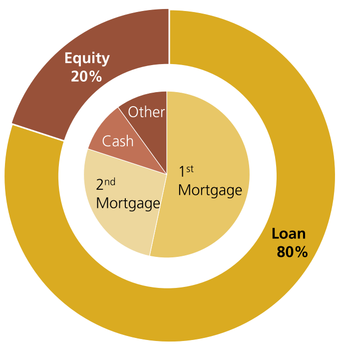
Mortgages are capped at 80% of a property's value

The norm in Switzerland is for purchases to be funded via a mix of mortgage borrowing and equity. However, mortgages may not exceed 80% of the purchase price. The first mortgage typically covers two-thirds of the property's value. A second mortgage then usually covers the difference up to 80% of the value and must be repaid on a linear basis over 15 years. A shorter amortization period may be required if the buyer will reach the age of retirement within 15 years.

Buyers must fund at least 20% of the purchase price with equity. Half of this amount (i.e. 10% of the purchase price) must consists of "hard" equity (e.g. savings, private pension assets such as pillar 3a, gifts, inheritance advances). The remaining 10% can come from occupational pension assets (pillar 2). Here again, stricter rules on the composition of equity apply if the buyer will reach the age of retirement within the next 15 years.

At least 20% of the purchase price must be funded from equity

Sources of funding, assuming the maximum possible mortgage, in %



Source: UBS

Size of mortgage is dependent on gross income

The maximum mortgage loan is dictated by the buyer's gross income. Their partner's income may only be taken into consideration if both partners will be jointly liable for the mortgage. Annual property ownership costs should not exceed one-third of gross annual income; these costs consist of mortgage interest costs (at a hypothetical interest rate of 5%) and maintenance and ancillary costs (each normally set at 1% of the value of the property). This is designed to ensure affordability even if interest rates rise significantly and to prevent debt exceeding five to six times gross annual income. Exceptions are possible based on wealth and personal circumstances.

Short-term versus long-term borrowing

For almost the whole of the last 20 years, the costs of money market financing have been below long-term financing costs. In line with market expectations, mortgage rates on short maturities have remained below those on long-term maturities. But the costs of hedging against sharp rises in interest rates in absolute terms are very low.

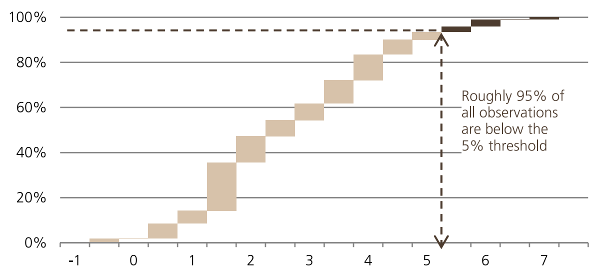
Choosing the right form of mortgage financing doesn't just depend on current interest rate expectations. It is also a question of the mortgage holder's risk capacity. When taking out a mortgage, you should ask yourself three questions:

- Could I cope with a very large increase in interest payments (interest rate risk)?

Even though a massive rise in interest rates is very unlikely, your property ownership costs should not exceed one-third of your gross annual income even if rates were to reach 5%.

Rates above 5% are a rarity

Frequency distribution for discount rates (1907–2000) and Libor rates (2001–2016)



Sources: SNB, UBS

- How much will it cost me to terminate my mortgage contract early (early cancellation risk)?

Paying off a mortgage early can be costly. The costs of exiting a mortgage contract depend on how lucratively the capital can be reinvested at that point in time. The lower interest rates are, the higher the exit costs. Conversely, if interest rates rise sharply, borrowers may even be rewarded for exiting the contract.

- How likely is it that I will have to renew my mortgage when interest rates are higher (refinancing risk)?

If the entire mortgage volume has to be refinanced at a higher rate, that will drive up the mortgage costs. For a borrower looking to minimize interest rate fluctuations, it can make sense to diversify long-term mortgages over time (by taking out a mix of fixed-term mortgages with different maturities). By contrast, refinancing risk is not a concern for holders of short-term mortgages.

Taxes and duties

It is important not to underestimate the taxes and duties payable when buying a property and during ownership. The total costs vary from canton to canton.

Taxation of the imputed rental value

The imputed rental value corresponds to the rental value of the owner-occupied property and is taxed as fictitious income. However, the property's mortgage interest payments and maintenance costs can be deducted from this theoretical income. In today's low interest rate environment, the imputed rental value frequently exceeds the deductible costs. An annual wealth tax must also be paid with respect to the property (after borrowing against the property), and some cantons also apply a separate property tax (which does not take borrowing into account).

Real estate gains tax and transfer tax

Two forms of tax are levied when a property is sold. Real estate gains tax can account for a large slice of the profit on the sale of a property if its value rose substantially during the period of ownership. As this tax is intended to curb property speculation, it decreases with length of ownership. For example, a real estate gain of CHF 100,000 in the canton of Zurich would attract tax of CHF 44,000 if held for less than one year. The same gain would be taxed at CHF 28,000 if held for five years, or CHF 15,000 after 20 years of ownership. The tax is deferred if the gain is used to buy another owner-occupied property. The second tax, real estate transfer tax, can be up to 3% of the purchase price. It is due at the time of purchase and—depending on the canton—is payable by the buyer, by the seller, or split 50/50 between the two. On top of that, notary costs must also be paid.

What does residential property in Switzerland cost?

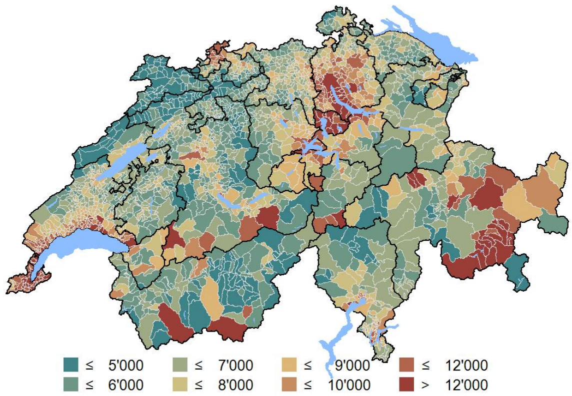
Prices

The highest prices are paid in the Lake Zurich and Lake Geneva areas and in the most sought-after Alpine tourist destinations. Prices in the high-end segment can often reach CHF 13,000 to CHF 15,000 per square meter in these regions. The CHF 20,000 per square meter mark is normal in the luxury segment.

Depending on factors including journey times to the nearest economic center, prices of CHF 8,000 to CHF 10,000 per square meter are typical in the high-end segment in metropolitan areas around Switzerland's larger cities. As a rule of thumb, prices fall by about 1% for every additional minute it takes to travel to the city center.

How much does residential property in Switzerland cost?

Prices per square meter in the high-end segment (70th percentile), in CHF, 1Q 2021



Sources: Wüest Partner, UBS

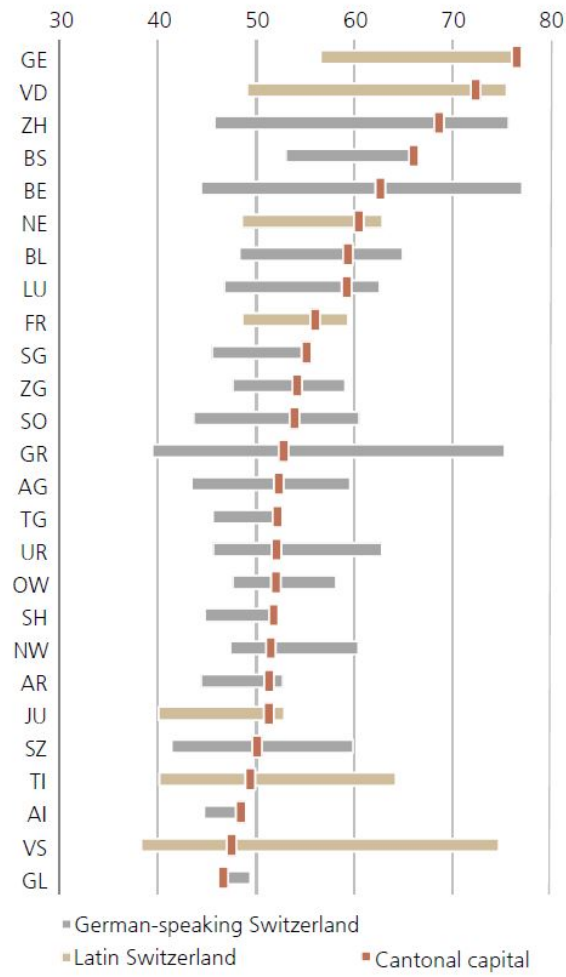
Living costs

Prices of owner-occupied homes are greatly influenced by the relative size of the local tax burden. If all location-related living costs are added together (ongoing residential property costs, taxes on income and wealth, and health insurance premiums), living in a 150 square meter condominium costs on average around CHF 52,500 per year across all Swiss municipalities.

However, there are sizeable differences between municipalities. For example, someone moving from the relatively low-tax municipality of Zug to a comparable apartment in the high-tax municipality of Montreux would face an increase in living costs of nearly 30%. In this case, annual costs would rise from around CHF 54,000 to nearly CHF 70,000. Overall, property prices tend to be higher in the lowest-tax municipalities, but this is balanced out by the smaller tax burden. The effect of this tax advantage is more evident for wealthier households.

Housing cost comparison condominiums

Range for all municipalities, in CHF thousand



Sources: FTA, FSO, Wüest Partner, UBS Assumptions: gross income of CHF 150,000, assets of CHF 250,000, married with two children, 150m2 condominium

Costs not related to financing

Whereas the financing costs associated with home ownership have consistently fallen over recent years, the share of expenses not directly related to financing has gone up. The home ownership costs not related to financing comprise operating (heating, electricity and water) costs, maintenance costs and investment costs (spending aimed at long-term value preservation). In absolute terms, the annual non-financing costs associated with a medium-sized condominium are likely to top CHF 10,000, although the total can fluctuate substantially from year to year. Good planning and targeted saving can help the joy of home ownership prevail over the headaches. The following table provides an estimate of annual non-financing costs.

Breakdown of costs per property type

Example calculation for a 150 square meter property of average quality; annual expenses or provisions in CHF

	Single family house		Owner-occ. apartment	
Operating costs	**3 700 -**	**5 100**	**3 000 -**	**4 100**
Maintenance costs	**4 000 -**	**5 500**	**3 600 -**	**5 000**
Heating & sanitary facilities	900 -	1 300	600 -	800
Roof	100 -	200	100 -	200
Diverse repairs	1 300 -	1 700	600 -	900
Lift			400 -	500
Surroundings & caretaker	1 700 -	2 300	1 900 -	2 600
Provisions for investments p.a.	**4 900 -**	**6 800**	**3 800 -**	**5 300**
Painting works	600 -	800	600 -	800
Bathroom/Kitchen	1 400 -	1 900	1 400 -	1 900
Floor covering	400 -	600	400 -	600
Heating system replacement	700 -	1 000	400 -	500
Electric installations	300 -	400	100 -	200
Windows/doors	400 -	600	200 -	300
Building envelope	1 100 -	1 500	700 -	1 000
Total	**12 600 -**	**17 400**	**10 400 -**	**14 400**

Source: UBS. No claim to completeness.

Price prospects

Prices to surge in short term

Prices in the Swiss residential real estate market have been surging since 2020. In the second quarter of 2021, they were some 5% above levels from a year earlier. Prices of single-family houses rose by 7% over the 12-month period, while condominiums went up by 2%. We expect the strong price momentum to persist this year.

- Despite a slight rise, low mortgage interest rates are supporting the residential property market, keeping demand and prices high. The ongoing costs associated with an owner-occupied home are currently estimated at 10–15% below those for a comparable rental property. This means, for example, someone living in a 150 square meter apartment would save around CHF 5,000 per year.

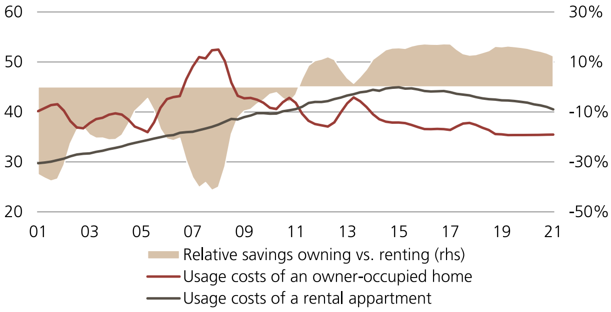
- We expect a strong economic recovery, which should improve many households' financial situations. Household purchasing power should also be boosted by asset price inflation.

- There are also solidly established expectations of long-term residential property appreciation, which have been cemented further by the experiences of the last few quarters.

- At present, the market is being buoyed by tight supply of available properties: Around 3.5% of all owner-occupied homes are currently advertised for sale. The latest statistics on building applications and permits do not point to a significant acceleration in the construction of new homes for owner occupation.

Low occupancy costs for owner-occupied homes

Nominal costs per square meter, per year for a new-build condominium and a comparable rental apartment in the high-end segment, smoothed



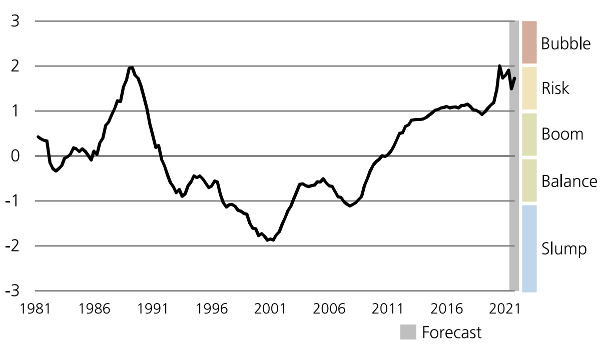
Sources: Wüest Partner, UBS * Mortgage interest payments for a long-term mortgage, provisions for maintenance and costs for imputed rental value taxation

Control mechanisms will curb demand in the long run

For most households, maximum purchase prices are constrained by affordability or lending criteria. Small apartments are therefore in increased demand, and relative willingness to pay for lower-quality properties remains high. Ultimately, however, price trends are closely tied to household incomes. This means Swiss real estate prices will only be able to continue their nearly 20-year rise if household incomes keep rising too. We therefore expect the pace of price increases to slacken from 2022.

The Swiss National Bank estimates that the residential property market is overvalued by between 5% and 30%. The *UBS Swiss Real Estate Bubble Index* is also closing in on bubble territory. There is no correction in sight at present, but a sharp rise in mortgage interest rates (e.g. by 1 to 2 percentage points) could trigger a 10–20% fall in property prices.

UBS Swiss Real Estate Bubble Index



Source: UBS

Vacation and luxury real estate

Demand for vacation and luxury properties remained high in the first half of 2021. Across tourism-dominated municipalities, prices of second homes rose by an average of just under 7% year-over-year. Prices were up by as much as 9% in luxury locations on Lakes Zurich and Geneva and in top Alpine destinations. These locations are benefiting not only from the drivers described above, but also from increased demand from beyond Switzerland's borders. This is because Swiss measures to control the pandemic have been significantly less restrictive than elsewhere, and the probability of tax hikes remains relatively low in view of the country's healthy public finances.

Further details on vacation property: UBS Alpine Property Focus

Further details on luxury property: UBS Luxury Property Focus

UBS Real Estate Local Fact Sheets

Finding a new home in a new country is a challenge. The *UBS Real Estate Local Fact Sheets* make this decision easier. They provide detailed information on local property prices, population trends, construction activity and taxes in all Swiss municipalities. You can obtain a copy from your UBS client advisor.

The largest residential property markets – a comparison

The 25 largest cities in Switzerland (by population)

Municipality	Can-ton	Price[1] Level	Price[1] Change	Population[2] Level	Population[2] Change	Tax burden[3]
Zürich	ZH	15 800	2.7	420 200	1.4	16.4
Genève	GE	16 900	7.6	204 000	0.8	20.5
Basel	BS	11 600	5.6	173 200	0.4	19.0
Lausanne	VD	13 300	6.9	139 400	0.4	21.5
Bern	BE	10 200	5.1	134 600	0.4	20.7
Winterthur	ZH	10 000	4.9	113 200	1.0	16.6
Luzern	LU	11 200	2.0	82 300	0.3	16.8
St. Gallen	SG	8 600	4.1	76 100	0.3	19.2
Lugano	TI	9 900	0.1	62 600	-0.7	18.0
Biel/Bienne	BE	6 600	2.4	55 600	0.7	21.0
Thun	BE	7 100	2.3	43 600	0.0	21.4
Bellinzona	TI	7 000	-0.6	43 300	0.3	19.2
Köniz	BE	8 100	2.0	42 000	0.9	20.5
Fribourg	FR	7 700	7.8	38 200	-0.5	19.7
La Chaux-de-Fonds	NE	4 500	0.5	37 500	-1.3	**22.9**
Schaffhausen	SH	7 500	4.4	36 600	0.4	17.5
Chur	GR	8 800	-1.9	36 000	0.6	16.6
Uster	ZH	12 000	4.2	35 000	0.7	15.9
Vernier	GE	12 500	9.9	35 000	0.0	20.9
Sion	VS	6 500	4.4	34 700	0.3	19.4
Neuchâtel	NE	7 800	0.5	33 500	-0.3	22.0
Lancy	GE	12 400	5.7	33 400	1.8	20.6
Emmen	LU	8 300	6.6	31 000	0.9	18.2
Zug	ZG	13 500	-0.7	30 600	0.9	**9.9**
Yverdon-les-Bains	VD	8 200	2.4	30 200	0.2	21.3

Source: UBS 1) Price in CHF/m2 for new-build properties (70th percentile) in 1Q 2021 and annualized rate of change since 1Q 2018; 2) Population in 2019 and annualized rate of change since 2016; 3) married without children with a gross income of CHF 200,000 p.a.

Appendix

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